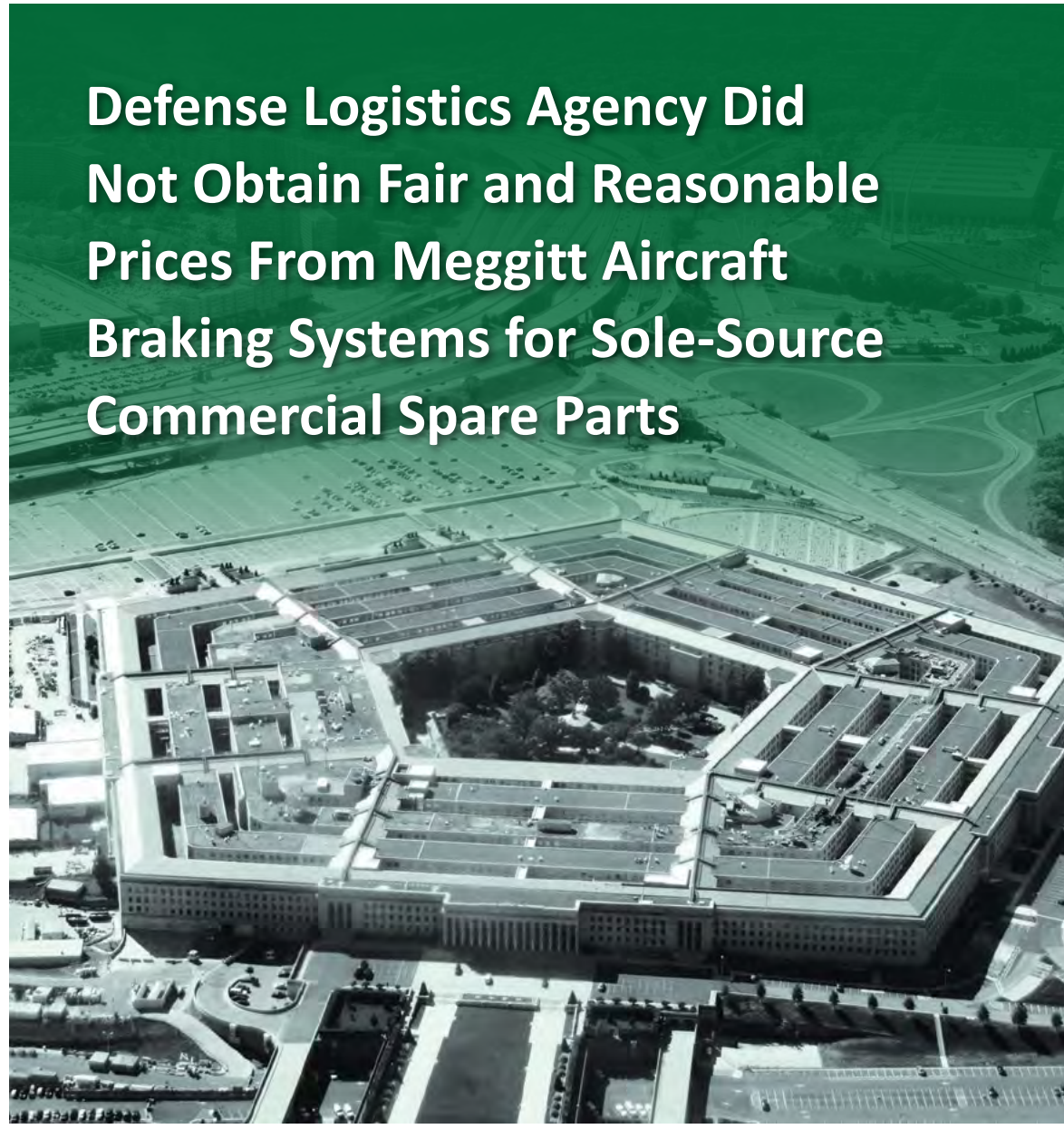


FOR OFFICIAL USE ONLY

INSPECTOR GENERAL

U.S. Department of Defense

MAY 8, 2015



Defense Logistics Agency Did Not Obtain Fair and Reasonable Prices From Meggitt Aircraft Braking Systems for Sole-Source Commercial Spare Parts

INTEGRITY ★ EFFICIENCY ★ ACCOUNTABILITY ★ EXCELLENCE

The document contains information that may be exempt from mandatory disclosure under the Freedom of Information Act.

FOR OFFICIAL USE ONLY

Report Documentation Page				Form Approved OMB No. 0704-0188	
Public reporting burden for the collection of information is estimated to average 1 hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to Washington Headquarters Services, Directorate for Information Operations and Reports, 1215 Jefferson Davis Highway, Suite 1204, Arlington VA 22202-4302. Respondents should be aware that notwithstanding any other provision of law, no person shall be subject to a penalty for failing to comply with a collection of information if it does not display a currently valid OMB control number.					
1. REPORT DATE 08 MAY 2015		2. REPORT TYPE		3. DATES COVERED 00-00-2015 to 00-00-2015	
4. TITLE AND SUBTITLE Defense Logistics Agency Did Not Obtain Fair and Reasonable Prices From Meggitt Aircraft Braking Systems for Sole-Source Commercial Spare Parts (REDACTED)				5a. CONTRACT NUMBER	
				5b. GRANT NUMBER	
				5c. PROGRAM ELEMENT NUMBER	
6. AUTHOR(S)				5d. PROJECT NUMBER	
				5e. TASK NUMBER	
				5f. WORK UNIT NUMBER	
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES) U.S. Department of Defense Inspector General, 4800 Mark Center Drive, Alexandria, VA, 22350-1500				8. PERFORMING ORGANIZATION REPORT NUMBER	
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)				10. SPONSOR/MONITOR'S ACRONYM(S)	
				11. SPONSOR/MONITOR'S REPORT NUMBER(S)	
12. DISTRIBUTION/AVAILABILITY STATEMENT Approved for public release; distribution unlimited					
13. SUPPLEMENTARY NOTES					
14. ABSTRACT					
15. SUBJECT TERMS					
16. SECURITY CLASSIFICATION OF:			17. LIMITATION OF ABSTRACT Same as Report (SAR)	18. NUMBER OF PAGES 56	19a. NAME OF RESPONSIBLE PERSON
a. REPORT unclassified	b. ABSTRACT unclassified	c. THIS PAGE unclassified			

INTEGRITY ★ EFFICIENCY ★ ACCOUNTABILITY ★ EXCELLENCE

Mission

Our mission is to provide independent, relevant, and timely oversight of the Department of Defense that supports the warfighter; promotes accountability, integrity, and efficiency; advises the Secretary of Defense and Congress; and informs the public.

Vision

Our vision is to be a model oversight organization in the Federal Government by leading change, speaking truth, and promoting excellence—a diverse organization, working together as one professional team, recognized as leaders in our field.



For more information about whistleblower protection, please see the inside back cover.



Results in Brief

Defense Logistics Agency Did Not Obtain Fair and Reasonable Prices From Meggitt Aircraft Braking Systems for Sole-Source Commercial Spare Parts

May 8, 2015

Objective

Our objective was to determine whether the Defense Logistics Agency (DLA) purchased sole-source commercial spare parts from Meggitt Aircraft Braking Systems (MABS) Corporation at fair and reasonable prices.

Finding

The DLA Aviation contracting officer did not obtain fair and reasonable prices for 51 of 54 statistically sampled sole-source commercial spare parts procured from the MABS companies. This occurred because the contracting officer did not conduct sufficient price analysis in accordance with federal and defense acquisition regulations. Specifically, the DLA Aviation contracting officer:

- relied on previous over-inflated contract prices to determine the 2013 contract prices;
- did not sufficiently analyze the “commercial of a type” parts¹ to determine whether the sales of comparable parts supported the contract prices;
- accepted excessive prices for new quantity ranges; and
- did not compare commercial sales to Government sales to determine whether sales were sufficient to support commercial part prices.

In addition, the contracting officer did not obtain cost data or perform a cost analysis on parts with prices that were not supported by the commercial sales data. The contracting officer also included language in a contract clause that limited DLA Aviation’s ability to fully negotiate

¹ Commercial of a type parts are items similar to those sold to the commercial market but have been slightly modified to meet DoD requirements

Finding (cont’d)

prices of parts added after the initial contract award.

As a result, DLA potentially overpaid MABS companies approximately \$8.5 of \$17 million paid for 32 sole-source commercial spare parts reviewed. In addition, DLA may overpay as much as \$70.5 million on 47 of 51 parts over the remaining term of the contract. When projected across the contract for all 5 years, DLA will overpay approximately \$106.8 of \$294.9 million (see Appendix E).

Recommendations

The Director, Defense Pricing, should issue guidance to establish a percentage of commercial sales that is sufficient to determine fair and reasonable prices when commercial items are acquired on a sole-source contract. In addition, the Director should assess and issue guidance to prohibit contracting officers from placing clauses in sole-source commercial contracts that limit DoD’s ability to obtain cost data.

The Director, DLA, should establish quality assurance processes to ensure that contracting officials elevate data request denials to the appropriate level. In addition, the Director should assess the contract clause that states cost data is not required and should review the contracting officer’s performance and, as appropriate, initiate administrative action.

The Director, DLA, should also require the contracting officer to establish fair and reasonable pricing for future parts added to the 2013 contracts and all future sole-source contracts with MABS for commercial parts by performing a thorough review of previous prices, sales data, and requesting “other than certified cost or pricing data,” to include cost data, when commercial sales data are not sufficient to determine fair and reasonable prices for sole-source commercial parts.

Management Comments and Our Response

The Director, Defense Pricing, and the Director, DLA Acquisition, responding for the Director, DLA, agreed with the recommendations. The comments addressed the specifics of the recommendations, and no further comments are required. Please see the Recommendations Table on the next page.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Director, Defense Pricing		1.a, 1.b
Director, Defense Logistics Agency		2.a, 2.b, 2.c, 2.d



**INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500**

May 8, 2015

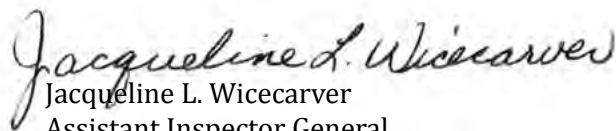
MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION,
TECHNOLOGY, AND LOGISTICS
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Defense Logistics Agency Did Not Obtain Fair and Reasonable Prices From
Meggitt Aircraft Braking Systems for Sole-Source Commercial Spare Parts
(Report No. DODIG-2015-120)

We are providing this report for your information and use. The Defense Logistics Agency did not obtain fair and reasonable prices for the Meggitt Aircraft Braking Systems companies' sole-source commercial spare parts. We determined that the Defense Logistics Agency potentially overpaid the Meggitt Aircraft Braking Systems companies about \$8.5 of \$17 million more than fair and reasonable prices for 32 sole-source commercial spare parts reviewed. In addition, Defense Logistics Agency may overpay as much as \$70.5 million on 47 of 51 parts over the remaining term of the contract. When projected across the contract for all 5 years, Defense Logistics Agency will overpay approximately \$106.8 of \$294.9 million (see Appendix E). We conducted this audit in accordance with generally accepted government auditing standards.

We considered management comments on a draft of this report when preparing the final report. Comments from the Director, Defense Pricing, and the Director, Defense Logistics Agency Acquisition, responding for the Director, Defense Logistics Agency, conformed to the requirements of DoD Instruction 7650.03; therefore, we do not require additional comments.

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 604-9077 (DSN 664-9077).


Jacqueline L. Wicecarver
Assistant Inspector General
Acquisition, Parts, and Inventory

Contents

Introduction

Objective	1
Background	1
Review of Internal Controls	4

Finding. DLA Aviation Did Not Obtain Fair and Reasonable Prices for Sole-Source Commercial Spare Parts 5

The Contracting Officer Did Not Obtain Fair and Reasonable Prices	5
Insufficient Price Analysis	6
Cost Data Not Obtained for Meggitt Aircraft Braking Systems Companies' Contracts	17
DLA Aviation Potential Overpayments	19
Management Comments on the Finding and Our Response	21
Recommendations, Management Comments, and Our Response	22

Appendixes

Appendix A. Scope and Methodology	27
Sales Analysis for Commercial Parts	28
Price Analysis for Commercial of a Type Parts	28
Cost Analysis	28
Price Analysis of Quantity Ranges	30
Use of Computer-Processed Data	30
Use of Technical Assistance	31
Appendix B. Prior Coverage	32
Appendix C. DLA Contracting Officials and DoD OIG Analysis Comparison	34
Appendix D. Cost Analysis of Meggitt Aircraft Braking System's Parts	36
Appendix E. Sampling Methodology	39

Management Comments

Defense Pricing	42
Defense Logistics Agency	43

Acronyms and Abbreviations 47

Introduction

Objective

Our objective was to determine whether the Defense Logistics Agency (DLA) purchased sole-source commercial spare parts from Meggitt Aircraft Braking Systems (MABS) Corporation at fair and reasonable prices. See Appendix A for a discussion of the scope and methodology and Appendix B for prior audit coverage related to the objective.

Background

DLA, headquartered at Fort Belvoir, Virginia, provides the Army, Marine Corps, Navy, Air Force, and combined and allied forces with a full spectrum of logistics, acquisition, and technical services. DLA also supplies more than 85 percent of the military's spare parts. DLA Aviation, headquartered in Richmond, Virginia, is the U.S. military's integrated materiel manager for more than 1.1 million repair parts and operating supply items in support of all fixed- and rotor-wing aircraft, including spares for:

- engines on fighters, bombers, transports and helicopters;
- all airframe and landing gear parts;
- flight safety equipment; and
- propeller systems.

Meggitt Aircraft Braking Systems

MABS, headquartered in Akron, Ohio, is a division of Meggitt PLC, a global engineering group headquartered in the United Kingdom. According to their website,² MABS is one of the world's leading aircraft wheel and brake suppliers on both military and commercial aircraft.

MABS parts include:

- brake control system units;
- landing gear computers;
- brake temperature sensors and monitoring units;
- main wheels;
- steel brakes;

² www.meggitt-mabs.com

- electric brakes;
- carbon brakes; and
- nose wheels.

Nasco Aircraft Brake Inc. is a wholly owned subsidiary of MABS and Meggitt, which supplies aircraft wheel and brake components for the military and commercial aircraft markets.

Nasco Aircraft Brake military aircraft parts include:

- stators;
- rotors;
- pistons;
- wear pads;
- backing plates;
- keys; and
- insulators.

Meggitt Aerospace is a United Kingdom subsidiary of Meggitt and conducts business as MABS. For purposes of the report, we will refer to the three companies as the MABS companies (MABS, Nasco Aircraft Brake, and Meggitt Aerospace).

Meggitt Aircraft Braking Systems Companies' Contracts

On April 2, 2007, DLA Aviation awarded a 5-year contract, SPM4A2-07-D-0006, to MABS³ for aircraft wheels, brakes, and spare parts. To allow more time to negotiate a follow-on contract with MABS, DLA Aviation awarded a 1-year contract, SPM4AX-12-D-9423, on September 1, 2012 (2012 contract).

On September 1, 2013, DLA Aviation awarded MABS a 5-year, firm-fixed-price, sole-source, indefinite-delivery requirements contract, SPE4AX-13-D-9418. In addition, DLA Aviation awarded contracts SPE4AX-13-D-9419 and SPE4AX-13-D-9420 to Nasco Aircraft Brake and Meggitt Aerospace, respectively. For purposes of this report, we will refer to these three contracts as the 2013 contracts. DLA Aviation initially awarded the 2013 contracts to supply 161 parts but have subsequently modified the contracts to add parts. As of July 1, 2014, the 2013 contracts included 249 parts, which for administrative purposes was valued at \$168.6 million.

³ In 2007, Meggitt purchased and combined Dunlop Aerospace Braking Systems Corporation and Aircraft Braking Systems Corporation to form MABS. The 2007 contract was awarded to Aircraft Braking Systems Corporation that subsequently became MABS.

The 2013 contracts included commercial spare parts that supported various aircraft, including the Boeing CH-47 Chinook helicopter and the Lockheed Martin F-16 Fighting Falcon. See Figure 1 for a picture of the CH-47 and F-16. Of the 249 parts on the 2013 contracts, 140 parts included quantity ranges with different prices for each range. For example, DLA could purchase 250 to 499 springs at a unit price of \$47.73 each or 500 or more springs at a unit price of \$34.83 each. As of November 30, 2014, DoD has ordered 148 of the 249 spare parts on contract, totaling \$33.1 million.



Commercial Item Definition

(FOUO) The Federal Acquisition Regulation (FAR) Subpart 2.1, “Definitions,” defines a commercial item as any item that has been sold or offered for sale to the general public. Additionally, the FAR considers an item similar to one sold to the commercial market, but has been slightly modified to meet DoD requirements as a commercial item. DoD refers to these items as “commercial of a type” parts.

[REDACTED]. The commercial parts included in the 2013 contracts are parts that are sold or offered for sale to the commercial market and are offered to the Government without any modifications.

Procedures for Pricing Commercial Items

FAR 15.402, “Pricing Policy,” states that contracting officers shall purchase supplies from responsible sources at fair and reasonable prices. When pricing commercial items, FAR 15.403-3, “Requiring Data Other Than Certified Cost or Pricing Data,” states that contracting officers must at least use price analysis to determine whether the prices are fair and reasonable. To establish fair and reasonable prices,

contracting officers shall obtain other than certified cost or pricing data,⁴ as necessary. FAR 15.402 states contracting officers should generally follow an order of preference when obtaining the data. The order of preference starts with data related to prices, such as catalog or market prices, and sales to non-governmental and governmental entities. The contracting officer must first rely on Government data, then on data obtained from sources other than the contractor. If fair and reasonable prices cannot be determined using that data, then the contracting officer shall request data from the contractor. The data obtained from the contractor shall include commercial sales data on the prices at which the same or similar items have been previously sold.

Defense Federal Acquisition Regulation Supplement (DFARS) Procedures, Guidance, and Information (PGI) 215.403-3, "Requiring data other than certified cost or pricing data," states that the sales data must be comparable to the quantities, capabilities, and specifications of the items proposed. If the sales data is not sufficient, additional data shall be obtained, including cost data, to the extent necessary to determine fair and reasonable prices.

Review of Internal Controls

DoD Instruction 5010.40, "Managers' Internal Control Program Procedures," May 30, 2013, requires DoD organizations to implement a comprehensive system of internal controls that provides reasonable assurance that programs are operating as intended and to evaluate the effectiveness of the controls. We identified internal control weaknesses for purchasing sole-source commercial spare parts from the MABS companies. The DLA Aviation contracting officer did not sufficiently conduct a price analysis in accordance with federal and defense acquisition regulations. Specifically, the contracting officer relied on previous over-inflated contract prices to determine the 2013 contract prices; did not sufficiently analyze the sales data for comparable parts of the commercial of a type parts on the 2013 contracts; accepted excessive prices for new quantity ranges; and included language to the 2013 contracts that limited DLA Aviation's ability to negotiate fair and reasonable prices. We will provide a copy of the report to the senior officials responsible for internal controls at the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics, and DLA.

⁴ The FAR defines other than certified cost or pricing data as pricing data, cost data, sales data, and judgmental information necessary for the contracting officer to determine a fair and reasonable price. Such data may include the same data as certified cost or pricing data but without the certification.

Finding

DLA Aviation Did Not Obtain Fair and Reasonable Prices for Sole-Source Commercial Spare Parts

The DLA Aviation contracting officer did not obtain a fair and reasonable price for 51 of 54 statistically sampled sole-source commercial spare parts procured from the MABS companies. This occurred because the contracting officer did not sufficiently conduct a price analysis in accordance with federal and defense acquisition regulations. In addition, the contracting officer did not obtain cost data or perform cost analysis on parts with prices that were not supported by the commercial sales data. As a result, DLA potentially overpaid approximately \$8.5 of \$17 million for 32 sole-source commercial spare parts reviewed. Additionally, DLA may overpay as much as \$70.5 million on 47 of 51 parts over the remaining term of the contract. When projected across the contract for all 5 years, DLA will overpay approximately \$106.8 of \$294.9 million (see Appendix E).

The Contracting Officer Did Not Obtain Fair and Reasonable Prices

The contracting officer did not obtain fair and reasonable prices for sole-source commercial spare parts procured from the MABS companies. FAR 15.402 requires contracting officers to award contracts with fair and reasonable prices. If fair and reasonable prices cannot be determined through other means, FAR 15.402(a)(2) requires contracting officers to obtain other than certified cost or pricing data necessary to establish fair and reasonable prices when certified cost or pricing data is not required.

When awarding a sole-source commercial contract, DFARS PGI 215.402(3) states that it is critical that contracting officers obtain sufficient data to support the proposed prices. Contracting officers can request Government and commercial sales history, cost data, or any other information required to determine fair and reasonable prices. Although the contracting officer determined fair and reasonable prices for the MABS contracts using Government and commercial sales data, we found that sales data we obtained from the MABS companies did not support the prices for 51 of 54 parts reviewed.⁵

⁵ (FOUO) The contracting officer reviewed [REDACTED] of 161 parts initially awarded. DLA Aviation added 88 parts to the contracts, since the initial contract award. We statistically sampled 54 of 182 parts from the MABS companies' 2013 contracts. See Appendix C for a summary of analysis techniques used.

Insufficient Price Analysis

The contracting officer did not conduct a sufficient price analysis in accordance with the federal and defense acquisition regulations. Specifically, the DLA Aviation contracting officer:

- relied on previous over-inflated contract prices to determine the 2013 contract prices;
- did not sufficiently analyze commercial of a type parts to determine whether prices were supported by sales of a comparable part;
- accepted excessive prices for new quantity ranges; and
- did not compare commercial sales to Government sales for commercial parts to determine if the prices were supported by sufficient commercial sales.

FAR 15.403-3 requires contracting officers to use, at a minimum, price analysis to determine whether prices are fair and reasonable. Price analysis is the process of evaluating a proposed price to determine fair and reasonable prices without evaluating its separate cost elements or profit. There are multiple price analysis techniques and procedures.

To conduct price analysis of commercial items, FAR 15.403-3(c)(1) requires contracting officers to obtain and review data showing the prices at which the same or similar items had been sold to DoD and the commercial market. DFARS PGI 215.402, "Pricing Policy," states that analyzing the sales data is particularly critical when sole-source commercial items are purchased. Had the contracting officer sufficiently analyzed the contractor's proposed prices, he may have concluded that fair and reasonable prices could not be determined using the data obtained from the contractor.

Reliance on Previous Over-Inflated Contract Prices

The contracting officer relied on previous over-inflated contract prices to determine the 2013 contract prices. DFARS PGI 215.403-3(4), "Reliance on prior prices paid by the Government," requires contracting officers to give extra attention to verify and document that sufficient analysis was performed to determine that prior prices were fair and reasonable. This is especially critical when the parts are acquired in a sole-source environment such as the 2013 contracts. At a minimum, contracting officers must discuss and document the basis of the previous prices paid with the contracting organization that previously bought the items.

(FOUO) To verify and document that sufficient analysis was performed to determine that prior prices were fair and reasonable, the contracting officer stated that [REDACTED]

[REDACTED]. In addition, the contracting officer reviewed [REDACTED]

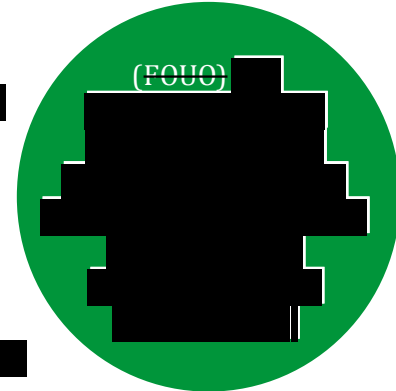
[REDACTED].⁷

(FOUO) The over-inflation is an indication that prices on previous contracts with the MABS companies were not fair and reasonable. However, [REDACTED]

[REDACTED]. The contracting officer [REDACTED]

[REDACTED]. Specifically, [REDACTED] to 152 parts from the 2012 contract [REDACTED]

[REDACTED]. [REDACTED]



Had the contracting officer questioned the previous contract's prices and determined they were not fair and reasonable because of the over-inflation, he may not have used those prices to calculate the 2013 contract's prices. The Director, DLA, should require the contracting officer to perform an adequate review of prior contract prices and establish pricing for all future contracts with MABS. The Director, DLA, should also conduct a review of the contracting officer's reliance on previous prices used to establish 2013 contract prices and determine if the contracting officer should have obtained additional data to determine fair and reasonable prices and initiate administrative action, if necessary.

Insufficient Analysis of Commercial of a Type Parts

The contracting officer did not sufficiently analyze sales data of comparable parts for commercial of a type parts⁸ on the 2013 contracts. To conduct price analysis on commercial of a type parts that could not be determined fair and reasonable through other techniques, DFARS PGI 215.403-3 requires contracting officers to obtain commercial sales data for the same or similar items that have

⁶ Intrinsic value is the established catalog or market price, plus the value of any unique requirements, including delivery terms, inspection, packaging, or labeling.

⁷ (FOUO) The DLA Aviation contracting officer [REDACTED]. MABS officials stated that [REDACTED].

⁸ Commercial of a type parts are items similar to those sold to the commercial market but have been slightly modified to meet DoD requirements.

been previously sold in comparable quantities adequate for determining price reasonableness. However, sales data for comparable parts provided by MABS companies were not adequate for determining the price reasonableness of the 35 contract commercial of a type parts of the 54 parts reviewed. We determined that the sales data did not have comparable prices or quantities for the parts on contract.

(FOUO) For example, [REDACTED]. The 2013 contract price for the nose wheel was \$27,273.72 for quantities ranging from 10 to 19 units.

(FOUO)
The 2013 contract price was [REDACTED] percent higher than the price of the commercial comparable part.

[REDACTED]. After inflating the comparable part's 2009 price and adding the contract price of the additional parts needed, we calculated that the 2013 contract price was \$ [REDACTED] ([REDACTED] percent) higher than the price of the commercial comparable part. Therefore, the 2013 contract price for the nose wheel could not be determined fair and reasonable using the commercial sales data provided by the MABS companies. Figure 2 shows the nose wheel.



Figure 2. Nose Wheel
Source: Air Force Materiel Command through DLA Distribution

(FOUO) Additionally, we reviewed the prices for a commercial of a type swage tube and the commercial sales data for a comparable part. The contracted minimum order quantity for the swage tube is 1,000 units at \$38.94 each. However, to justify the swage tube's price, MABS officials provided commercial sales data for a comparable swage tube that indicated they had only sold [REDACTED] units to commercial customers from [REDACTED]. Therefore, the sales price of the [REDACTED] units could not be compared to the price of 1,000 units that would have been purchased on the MABS 2013 contract because MABS had not sold the comparable swage tube in a comparable quantity. Consequently, a fair and reasonable price could not be determined based on the commercial sales data. Figure 3 shows the swage tube.

Had the contracting officer sufficiently analyzed the comparable parts' sales data provided by the MABS companies for the commercial of a type parts, he may have concluded that the comparable parts' data did not support the contract prices or quantities. The Director, DLA should require DLA Aviation contracting officers to establish fair and reasonable pricing for all future sole-source contracts with the MABS companies for commercial of a type parts by adequately reviewing sales data and, when necessary, request other than certified cost or pricing data to include cost data when the commercial sales data is not sufficient to determine fair and reasonable prices. Additionally, the Director, DLA, should review the contracting officer's performance for conducting price analysis of the commercial of a type parts on the contracts with the MABS companies and, as appropriate, initiate administrative action.



Figure 3. Swage Tube
Source: DLA Distribution

The Contracting Officer Accepted Excessive Prices for New Quantity Ranges

The contracting officer accepted excessive prices that the MABS companies proposed for new quantity ranges added in the 2013 contracts. The contracting officer requested and MABS provided quantity ranges with different prices for 140 of the 249 parts on the 2013 contracts. According to contracting officials, DLA expects prices to decrease 5 percent every time the quantity produced doubles due to manufacturing efficiencies. For the 2013 contracts, the contracting officer stated that DLA requested the quantity ranges to obtain lower prices for purchasing higher quantities of parts. Instead, the quantity ranges substantially increased the prices for purchasing lower quantities of parts.

(FOUO) The contracting officer obtained new quantity ranges⁹ for 36 of 140 parts on the 2013 contracts. Of the 36 parts with new quantity ranges, 30 added ranges to purchase lower quantities of parts than previously available.

The contracting officer... stated that the MABS companies refused to lower their prices.

The contracting officer [REDACTED]
[REDACTED]
[REDACTED]. However, the MABS companies [REDACTED]
[REDACTED] for the new lower quantity ranges. The contracting officer [REDACTED]
[REDACTED]
[REDACTED] and stated that the MABS companies refused to lower their prices.

(FOUO) For example, DLA could only purchase 100 or more pins on the 2012 contract at \$83.41 each. The contracting officer [REDACTED]
[REDACTED] from 172 parts per year on the 2012 contract to 16 parts per year on the 2013 contract. The MABS companies complied and added two quantity ranges to purchase the pins in lower quantities. The contracting officer [REDACTED]
[REDACTED] than the MABS companies offered but [REDACTED]
[REDACTED] and added annual inflation, which increased the prices further.

Therefore, to purchase 25 to 49 units on the 2013 contracts, DLA would pay \$293.26 each, a 251.6 percent increase from the 2012 contract price. This was higher than the 5 percent that the contracting officials stated they would expect. See Table 1 for the cost of the pins based on the quantity ranges and Figure 4 shows a picture of the pin.

⁹ We only considered parts that were included on both the 2012 contract and the 2013 contracts with the MABS companies, when identifying new quantity ranges.

Table 1. New Quantity Ranges for a Pin

2012 Contract		2013 Contract		Price Increase (Percent)
Quantity Range	Unit Price	Quantity Range	Unit Price	
		25–49*	\$293.26	251.6
		50–99	155.44	86.4
≥100	\$83.41	≥100	86.54	3.8

* DLA estimates an annual demand of 16 units per year.



Figure 4. Pin
Source: DLA Distribution

(FOUO) In another example, DLA could purchase “any” quantity (one or more) of a brake assembly on the 2012 contract for \$5,425.25 each. The contracting officer [REDACTED]. Therefore, MABS changed the purchasing quantity of “any” and added three quantity ranges to purchase the parts in quantities of 5, 10, and 25. DLA obtained a comparable price when purchasing 25 or more units at \$5,628.81 each.¹⁰ The contracting officer [REDACTED] for the new quantity ranges but [REDACTED] before adding additional annual inflation to the prices. Therefore, to purchase as few as five to nine units, DLA will pay \$8,219.19 each, a 51.5 percent increase from the 2012 contract price. See Table 2 for the cost of the brake assemblies based on the quantity ranges and Figure 5 shows a picture of the brake assembly.

¹⁰ We determined that the unit price for purchasing 25 or more parts, \$5,628.81, was comparable because it is approximately 3.8 percent more than the 2012 contract unit price of \$5,425.25.

Table 2. New Quantity Ranges for a Brake Assembly

2012 Contract		2013 Contract		Price Increase (Percent)
Quantity Range	Unit Price	Quantity Range	Unit Price	
1 or more	\$5,425.25	5–9	\$8,219.19	51.5
		10–24	6,600.21	21.7
		≥25*	5,628.81	3.8

* DLA estimates an annual demand of 34 units per year.



Figure 5. Brake Assembly
Source: DLA Distribution

(FOUO) Furthermore, the estimated annual demand for a duplex snap button decreased from 853 parts per year on the 2012 contract to 447 parts per year on the 2013 contract. The contracting officer [REDACTED], which the MABS companies provided. However, the MABS companies [REDACTED] for the lower quantity ranges. The contracting officer counter offered with prices that aligned with DLA's expectation of a 5 percent decrease in prices when quantities double, but the contracting officer ultimately accepted MABS' prices.

Therefore, DLA could purchase the duplex snap button on the 2013 contract in five different quantities at different prices. Specifically, DLA could purchase 2,500 or more at \$7.81 each, or it could purchase 100 to 249 at \$44.59 each—a 470.9 percent price increase from the lowest quantity range to the highest. See Table 3 for the cost and percentage increase of the duplex snap button based on the quantity ranges and Figure 6 shows a picture of the duplex snap button.

Table 3. Quantity Range Increases for a Duplex Snap Button

2012 Contract		2013 Contract		Price Increase for Each 2013 Range (Percent)	Price Increase From Lowest to Highest 2013 Price (Percent)
Quantity Range	Unit Price	Quantity Range	Unit Price		
		100–249	\$44.59	138.4	470.9
		250–499*	18.70	48.1	
500–999	\$12.17	500–999	12.63	31.7	
1,000–2,499	9.25	1,000–2,499	9.59	22.8	
≥2,500	7.52	≥2,500	7.81		

* DLA estimates an annual demand of 447 units per year.



Figure 6. Duplex Snap Button
Source: DLA Distribution

Although the contracting officer attempted to negotiate quantity range prices that aligned with DLA's expectation of manufacturing efficiencies, the contracting officer ultimately accepted the higher prices proposed by the MABS companies. Had the contracting officer questioned the new prices further, he may have obtained additional data to support the proposed prices, such as other than certified cost or pricing data, which could include cost data. The Director, DLA, should require the contracting officer to establish and negotiate fair and reasonable pricing on all future contracts with the MABS companies by conducting sufficient price analysis and requesting other than certified cost or pricing data, which could include cost data, when prices cannot be determined fair and reasonable by other means. Additionally, the Director, DLA, should review the contracting officer's price analysis of the quantity ranges and initiate administrative action, as appropriate.

Insufficient Sales Data Analysis

The contracting officer did not compare the commercial sales to the Government sales for the 19 commercial parts¹¹ of the 54 parts reviewed to ensure that the prices were supported by sufficient commercial sales. DFARS PGI 215.402 states that obtaining sufficient data from the contractor, including sales data of items sold in similar quantities, is particularly critical for the acquisition of commercial items on a sole-source basis. DFARS PGI 215.404-1(a)(iii) adds that when procuring sole-source commercial items, the contracting officer must obtain additional data when the sales data is not sufficient to support a fair price. The contracting officer stated he only reviewed sales data for a sample of parts to confirm that commercial sales existed, but he did not review the sales data to determine whether commercial sales were similar to Government sales.

Currently, there is no official guidance that establishes a sufficient percentage of commercial sales to support fair and reasonable price determinations. A previous DoD OIG report¹² identified overpricing when contracting officers relied on a market-based pricing strategy when sufficient commercial market sales did not exist. The report recommended the Director, Defense Pricing, issue guidance to establish a percentage of commercial sales that was sufficient to determine fair and reasonable prices when commercial items were acquired on a sole-source basis.

¹¹ The commercial parts reviewed are parts that are sold or offered for sale to the commercial market and are offered to the Government without any modifications.

¹² DODIG-2014-088, "Defense Logistics Agency Aviation Potentially Overpaid Bell Helicopter for Sole-Source Commercial Spare Parts," July 3, 2014.

The Director agreed with the recommendation and planned to issue guidance. At that time, the Director preliminarily stated that he considered 50 percent or more commercial sales as sufficient to accept market prices when determining fair and reasonable prices.

On February 4, 2015, the Director, Defense Pricing issued guidance about using market-based pricing, but the policy did not establish a percentage of commercial sales that was sufficient to determine fair and reasonable prices. However, on January 14, 2015, a Defense Procurement and Acquisition Policy representative stated that a DFARS change with a percentage was warranted in the future. The Director, Defense Pricing, should issue guidance to establish a percentage of commercial sales that is sufficient to determine fair and reasonable prices when commercial items are acquired on a sole-source contract.

Based on our established approach and previous discussions with the Director, Defense Pricing, we identified commercial parts with commercial sales of less than 50 percent of their total sales as insufficient to accept prices as fair and reasonable. For the 19 commercial parts we reviewed, we compared the commercial sales to the Government sales to determine which prices the commercial market supported and which prices required additional data to support the prices. We identified that 16 of 19 parts had commercial sales that were less than 50 percent of the Government sales during a 5-year period prior to contract award. Specifically, commercial sales for the 16 parts ranged from 0 percent to 42.1 percent of total sales. See Table 4 for the 16 of 19 parts with less than 50 percent commercial sales. Therefore, based on our methodology, these parts did not have sufficient commercial sales to accept the prices as fair and reasonable without additional supporting documentation.

For example, on the 2013 contracts one part had only 3.3 percent commercial sales and another part had only 7.6 percent commercial sales during the 5-year period. The data showed that the commercial sales were not sufficient to support the prices, and the contracting officer should not have accepted the prices as fair and reasonable based on the data provided by the MABS companies.

Table 4. Analysis of Commercial to Government Sales

Parts		Sales Comparison (5-year period)	
NSN	Name	Commercial Sales (Percent)	Government Sales (Percent)
5310-01-222-4119	Washer	0	100
1630-01-003-8538	Stator	3.3	96.7
1630-00-937-6602	Rotor	7.6	92.4
1630-01-005-4188	Press Plate	8.5	91.5
5310-00-950-1292	Nut	11.0	89.0
1630-00-899-5782	Bushing	17.0	83.0
1630-00-022-3074	Stator	19.5	80.5
1650-00-102-4364	Boot	20.4	79.6
1630-01-037-4960	Grip	21.9	78.1
1630-01-189-8644	Disk	22.6	77.4
1630-01-523-6203	Parts Kit for Disk	34.0	66.0
5330-01-196-2451	Seal	38.3	61.7
1630-01-033-4606	Disk	39.2	60.8
1630-01-009-8474	Wheel	39.8	60.2
1630-00-899-5783	Adapter	40.2	59.8
1630-01-047-7335	Disk Brake	42.1	57.9
1630-99-257-3586	Fusible Plug	82.4	17.6
5310-00-264-0640	Nut	95.6	4.4
1630-01-517-4129	Brake	100	0

Cost Data Not Obtained for Meggitt Aircraft Braking Systems Companies' Contracts

The contracting officer did not obtain cost data to perform cost analysis on sole-source commercial spare parts with prices that were not supported by the commercial sales data. In addition, the contracting officer included language in the 2013 contracts limiting DLA's ability to obtain cost data when negotiating additional parts added to the 2013 contracts.

DFARS PGI 215.402 emphasizes that if the commercial sales data for commercial sole-source items are not sufficient for determining fair and reasonable prices, then cost data should be requested. As previously discussed, the commercial sales data the MABS companies provided the audit team did not support the contract prices for 51 of 54 parts reviewed. Specifically, based on our established approach, commercial sales for 16 of 19 commercial parts reviewed did not have sufficient commercial sales to accept their prices. In addition, sales data for comparable parts for the remaining 35 commercial of a type parts reviewed did not support the contract prices. Therefore, the contracting officer should have requested additional information, such as uncertified cost data, to determine fair and reasonable prices for the 51 parts reviewed.

Contracting Officials Did Not Elevate Cost Data Denials

(FOUO) The contracting officer stated he did not request cost data from the MABS companies to further support the proposed prices of specific parts because the MABS companies had historically refused to provide cost data to DoD to support their commercial parts prices. Specifically, [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]. In response, a MABS official stated [REDACTED]
[REDACTED]
[REDACTED].

MABS companies had historically refused to provide cost data to DoD.

Therefore, DLA contracting officials knew before entering negotiations that the MABS companies would not provide cost data to support their prices and did not request uncertified cost data even though the FAR and DFARS permit it. According to DLA contracting officials, they determined fair and reasonable prices without obtaining uncertified cost data from the MABS companies.

The contracting officials should have elevated the MABS companies' persistent denials to provide cost data to the DLA Aviation Head of the Contracting Activity. The FAR and DFARS provide guidance for situations when the contractor does not comply with a requirement to submit data. Specifically, DFARS PGI 215.404-1(a)(i) states that contracting officers should elevate any denials of data requests to the appropriate officials, which could include the Head of the Contracting Activity.

In addition, FAR 15.403-3(a)(4) states that if a contractor continues to deny the requested data, the contractor is ineligible for contract award unless the Head of the Contracting Activity determines the award of the contract is in the best interest of the Government. DLA contracting officials stated that the MABS companies' denials of cost data were not elevated to the Head of Contracting Activity because the MABS companies have consistently refused to provide cost data, even when requests were elevated to the Head of Contracting Activity during negotiations of a previous 2007 contract. The Director, DLA, should establish quality assurance processes to ensure contracting officials elevate data request denials to the appropriate level to resolve the problem, including the Head of the Contracting Activity, as required by the DFARS.

The Contracting Officer Limited DLA's Ability to Obtain Cost Data

(FOUO) The contracting officer limited DLA's ability to obtain cost data when additional parts are negotiated and added to the 2013 contracts. Specifically, FAR clause 52.215-21¹³ allows contracting officers to insert the description of the data required to adequately evaluate the proposed prices. When negotiating the contract, the MABS company officials requested [REDACTED]

[REDACTED]. As a result, the contracting officer inserted the following statement into the clause: "Cost data of any kind is not required under this contract."

The contracting officials stated that this clause did not prohibit DLA from requesting cost data, and the inclusion of the clause in the 2013 contracts did not have an effect because MABS companies had always refused to provide cost data. A DLA official stated that the inclusion of this clause was a "no-cost solution" to settle the concerns raised by the MABS companies, which enabled the 2013 contracts to be awarded. However, FAR 15.403-3(c) and DFARS PGI 215.402(3) permit contracting officers to obtain other than certified cost or pricing data, which

¹³ FAR Cause 52.215-21, "Requirements for Certified Cost or Pricing Data and Data Other Than Certified Cost or Pricing Data—Modifications"

includes cost data, for commercial items, and the DFARS PGI states it is critical to obtain this data when sole-source commercial items are procured. Therefore, including the clause in the 2013 contracts limited DLA Aviation's ability to fully negotiate fair and reasonable prices for all parts added to the 2013 contracts after the initial award.

(FOUO) Additionally, a MABS company official stated that [REDACTED]
[REDACTED]
[REDACTED],
initially worth approximately \$149.4 million. And, when a contracting specialist [REDACTED], a MABS official [REDACTED].

Contracting officials subsequently added 88 parts to the 2013 contracts after initial award from October 30, 2013, through July 1, 2014. During negotiations for those parts, contracting officials could not contractually request cost data. The Director, DLA, should assess and determine if the alternate language added to FAR clause 52.215-21 in the 2013 contracts is appropriate. If the language is not appropriate, initiate actions as necessary, to include requiring the contracting officer to modify the clause in the three contracts with the MABS companies. In addition, the Director, Defense Pricing should assess and issue guidance prohibiting contracting officers from placing clauses in sole-source commercial contracts limiting DoD's ability to obtain cost data. Finally, the Director, DLA, should review the contracting officer's decision to include language in the 2013 contracts that limited DLA's ability to determine fair and reasonable prices of parts added to the contracts after initial award and initiate administrative action, as appropriate.

DLA Aviation Potential Overpayments

As a result, DLA Aviation potentially overpaid the MABS companies approximately \$8.5 of \$17 million for 32 sole-source commercial spare parts procured from September 1, 2013, through November 30, 2014. Of the 51 parts, we identified 3 parts in which MABS companies received a lower profit.¹⁴ For these three parts, the MABS companies lost \$109,344. As of November 30, 2014, DoD has not purchased 16 of 51 parts reviewed.

¹⁴ We applied a profit range obtained from the DLA Aviation contracting officer's weighted guidelines calculation.

Using the contracts' estimated annual demand quantities, we determined that over the remaining term of the contract, DLA Aviation may potentially overpay the MABS companies as much as \$70.5 million for 47 of 51 parts reviewed. When projected across the contract for all 5 years, DLA will overpay approximately \$106.8 of \$294.9 million.¹⁵

(FOUO) For example, a brake disc has a weighted average price¹⁶ of \$2,314.26. We performed cost analysis and determined that a fair and reasonable weighted average price for this brake disc is \$[REDACTED]. From September 1, 2013, through November 30, 2014, DLA Aviation procured 767 units, potentially overpaying about \$[REDACTED] ([REDACTED] percent). Using the estimated annual demand quantity of 445 units,¹⁷ DLA Aviation will potentially overpay about \$[REDACTED] ([REDACTED] percent) over the remaining term of the contract. Figure 7 shows the disc brake. See the table in Appendix D for the cost analysis of the 35 parts.

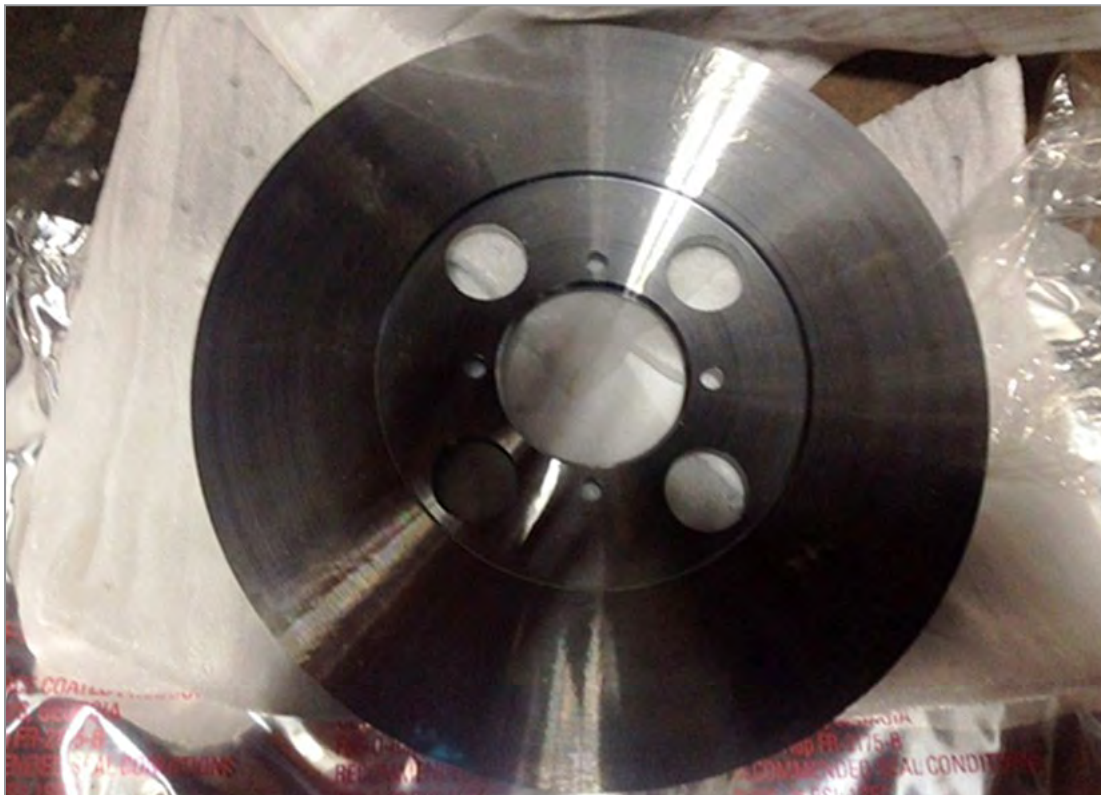


Figure 7. Disc Brake
Source: DLA Distribution

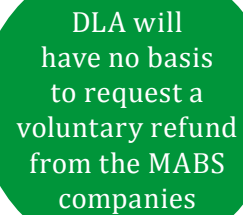
¹⁵ See Appendix E for discussion.

¹⁶ See Footnotes 3 and 4 of the Table in Appendix D for an explanation of the weighted average price calculations used for cost analysis.

¹⁷ The audit team used the estimated annual demand from a parts list obtained from DLA on May 8, 2014.

Had the contracting officer followed the FAR and the DFARS provisions for the acquisition of commercial sole-source items, DLA Aviation could have ensured that the prices agreed to in the contract were fair and reasonable. In cases like this, we normally would recommend the Director, DLA request a voluntary refund of the approximately \$8.5 million of excess payments made to the MABS companies. However, the 2013 contracts are 5-year, long-term contracts with no option years and no renegotiation or most favorable customer clauses. In addition, the contract clause stating that “cost data of any kind is not required” limits DLA’s ability to obtain cost data necessary to calculate an overpayment amount.

Without access to the data necessary to calculate an overpayment, DLA will have no basis to request a voluntary refund from the MABS companies or renegotiate the previous prices in the 2013 contracts with the MABS companies. Therefore, we are not recommending DLA request a voluntary refund or renegotiate previous prices paid. The Director, DLA, should require the contracting officer to assess and implement contractual actions available to negotiate prices for future parts added to the 2013 contracts with the MABS companies and all future sole-source contracts with MABS for commercial parts by performing a thorough review of prior prices, sales data, and requesting other than certified cost or pricing data, to include cost data, when commercial sales data are not sufficient to determine fair and reasonable prices for sole-source commercial parts.



DLA will have no basis to request a voluntary refund from the MABS companies

Management Comments on the Finding and Our Response

The Director, DLA Acquisition commented on several initiatives DLA has implemented responding to DoD OIG audits. He stated that in December 2014, he issued “Guidance on Determining Sole Source Commercial Prices Fair and Reasonable,” which established a 40-percent non-Government sales threshold as a sufficient percentage of sales supporting fair and reasonable price determinations. In addition, the guidance established a requirement that there be at least five sales in the prior 3 years as a basis for using commercial sales for price reasonableness determinations.

The Director also stated that DLA reviewed 192 contract files for sole-source contracts and determined that additional education and training is needed for the DLA acquisition workforce. The Director stated that his office worked with the Defense Acquisition University and created a DLA specific cost and pricing training course titled, "Determining Price Reasonableness Using Price and Cost Analysis Methods." He further explained that the course focuses on areas including market research, sole-source commercial pricing, price and cost analysis techniques, escalation methods, and analysis and learning curves.

Finally, the Director stated DLA is creating an in-house Enterprise Pricing Tool Suite that will provide support tools to the workforce for cost and price analysis. The system will include weighted guidelines, price indices, pricing history analysis, and rare market price volatility.

Our Response

We commend DLA for implementing these initiatives addressing problems with determining fair and reasonable prices for sole-source commercial items.

Recommendations, Management Comments, and Our Response

Recommendation 1

We recommend that the Director, Defense Pricing:

- a. **Issue guidance to establish a percentage of commercial sales that is sufficient to determine fair and reasonable prices when commercial items are acquired on a sole-source contract.**

Defense Pricing Comments

The Director, Defense Pricing, agreed, stating that DoD is developing a proposed DFARS rule that will contain a definition of "market-based pricing." The Director anticipates that the rule will include a percentage of commercial sales that is sufficient to determine whether the prices are fair and reasonable when commercial items are procured on a sole-source basis. The Director stated that the rule change is case 2013-D0034, "Evaluating Price Reasonableness for Commercial Items."

Our Response

Comments from the Director meet the intent of the recommendation; therefore, no further comments are required.

- b. Assess and issue guidance prohibiting contracting officers from placing clauses in sole-source commercial contracts limiting their ability to obtain cost data.**

Defense Pricing Comments

The Director, Defense Pricing, agreed, stating that he intends to include language in the DFARS rule change 2013-D0034, "Evaluating Price Reasonableness for Commercial Items," to prohibit contracting officers from placing clauses in sole-source commercial contracts that will limit their ability to obtain cost data. The Director stated that the current text complies with our recommendation.

Our Response

Comments from the Director meet the intent of the recommendation; therefore, no further comments are required.

Recommendation 2

We recommend that the Director, Defense Logistics Agency:

- a. Review the performance of the Defense Logistics Agency Aviation contracting officer for contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420 to determine if sufficient price analysis was conducted and if inclusion of language in the contracts restricting cost data limited Defense Logistics Agency's ability to determine fair and reasonable prices. Based on the results of the review of the contracting officer's actions, initiate administrative action, as appropriate.**

Defense Logistics Agency Comments

The Director, DLA Acquisition, responding for the Director, DLA, agreed, stating that he reviewed the pricing related documents for the 2013 contracts and determined sufficient price analysis was conducted to properly determine the prices fair and reasonable. Specifically, he stated the documentation showed the contracting officer's review and methodology for price analysis was appropriate. In addition, the Director stated that he reviewed the contract clause in the 2013 contracts and determined that it did not limit DLA's ability to determine fair and reasonable prices. Therefore, the Director, DLA Acquisition stated that no action was required for this recommendation.

Our Response

While the Director agreed with the recommendation, we do not agree the contracting officer determined fair and reasonable prices. As stated in our report, the contracting officer did not conduct a sufficient price analysis in accordance with the federal and defense acquisition regulations because he relied on previous over-inflated contract prices; did not sufficiently analyze sales data for comparable parts of the commercial of a type parts; and accepted excessive prices for new quantity ranges.

We also do not agree that the contract clause did not limit DLA's ability to determine fair and reasonable prices. Officials at Defense Pricing agreed that including language in a contract clause, which limited DLA's ability to obtain cost data, was inappropriate. Specifically, the Director, Defense Pricing, plans to add language to the DFARS prohibiting contracting officers from placing clauses in sole-source commercial contracts that limit their ability to obtain cost data.

Although we disagree that the contracting officer adequately determined fair and reasonable prices, comments from the Director addressed the specifics of the recommendation by conducting a review of the contracting officer's actions. Therefore, no further comments are required.

- b. Establish a quality assurance process to ensure when requests for contractor data is denied, contracting officers follow the procedures in Defense Federal Acquisition Regulation Supplement Procedures, Guidance, and Information 215.404-1(a), which requires contracting officials to elevate data request denials to the appropriate level to resolve the problem, including the Head of the Contracting Activity.**

Defense Logistics Agency Comments

The Director, DLA Acquisition, responding for the Director, DLA, agreed, stating that DLA has a quality assurance process in place in the DLA Acquisition Directive. Specifically, DLA Acquisition Directive 15.405(a)(S-90) states the offeror's refusal to provide cost or pricing data or other-than-cost or pricing data does not relieve the contracting officer from the requirement to perform a proposal analysis or provide a sufficient basis to determine if a price is fair and reasonable or unfair and unreasonable. In such instances, the guidance in 15.404-2(d) applies in the case of failure to provide other than cost or pricing data. DLA Acquisition Directive 15.404-2(d)(S-90) states in the event the contracting officer and higher management are unsuccessful in obtaining the data, the matter shall be elevated, after review by the local pricing and contract review elements, to the Head of the

Contracting Activity. The Director stated that since the contracting officer properly determined the prices fair and reasonable through price analysis, the process to elevate the denial of requested data in DFARS PGI 215.404-1(a) was not applicable.

Our Response

While the Director agreed with the recommendation, we do not agree the contracting officer determined fair and reasonable prices. Although the Director stated that the contracting officer properly determined fair and reasonable prices through price analysis, the DLA Aviation Procurement Director requested cost data from the MABS companies, stating that the contracting officer could not determine fair and reasonable prices based on the data available to them. Subsequently, the MABS companies denied the request. Therefore, in accordance with the procedures in DLA Acquisition Directive 15.404-2(d)(S-90), the MABS companies' denial of cost data should have been elevated to the DLA Aviation Head of Contracting Activity.

While we disagree with the Director's review of the contracting officer's actions, the procedures to elevate data request denials are included within DLA Acquisition Directive 15.404. Therefore, no further comments are required.

- c. Assess contract clause 52.215-21, "Requirements for Certified Cost or Pricing Data and Data Other Than Certified Cost or Pricing Data," included in contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420 and determine whether the statement, "cost data of any kind is not required under this contract," is appropriate and, if not, initiate actions as necessary that requires the Defense Logistics Agency Aviation contracting officer to modify the contracts to remove the statement.**

Defense Logistics Agency Comments

The Director, DLA Acquisition, responding for the Director, DLA, agreed, stating that DLA assessed the statement "cost data of any kind is not required under this contract," and determined the language was appropriate in the circumstances of this procurement. Specifically, he stated the FAR clause authorizes the contracting officer to insert language to describe the data required. He stated that according to the clause and regulatory guidance, the type of data to be submitted, is left to the contracting officer's discretion. The Director explained that the language in the contracts simply reflected the parties' agreement that only commercial items with prices could be determined fair and reasonable based on sales data, without the need for cost data, would be added to the contracts. He stated that since the language is appropriate and the contracting officer obtained sufficient noncost data to determine the prices fair and reasonable, it was not necessary to negotiate with MABS to modify the contracts to remove the statement.

Our Response

While the Director agreed with the recommendation, we do not agree that the statement, “cost data of any kind is not required under this contract,” is appropriate and officials at Defense Pricing agree. Specifically, the Director, Defense Pricing, plans to add language to the DFARS that prohibits contracting officers from placing clauses in sole-source commercial contracts, which limits their ability to obtain cost data. However, the Director’s comments meet the intent of the recommendation because DLA assessed the statement and determined whether it was appropriate. Therefore, no further comments are required.

- d. Require the Defense Logistics Agency Aviation contracting officer to establish fair and reasonable pricing for future parts added to contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420, and all future sole-source contracts with Meggitt Aircraft Braking Systems for commercial parts to include performing a thorough review of prior prices, sales data, and requesting other than certified cost or pricing data, to include cost data when commercial sales data are not sufficient to determine fair and reasonable prices for sole-source commercial parts.**

Defense Logistics Agency Comments

The Director, DLA Acquisition, responding for the Director, DLA, agreed, stating that DLA contracting personnel will follow all current and future applicable FAR, DFARS, and DLA Acquisition Directive policies and procedures to establish fair and reasonable pricing for future parts added to the 2013 contracts and all future sole-source contracts with MABS for commercial parts. Specifically, the Director stated that DLA contracting personnel will follow all applicable guidance, including DLA’s “Guidance on Determining Sole Source Commercial Prices Fair and Reasonable,” December 16, 2014. In addition, the Director stated DLA will consider requesting assistance from the Defense Contract Management Agency Cost and Pricing Center for future acquisitions. Additionally, the Director stated DLA will follow the Office of the Under Secretary of Defense, Acquisition, Technology, and Logistics Memorandum, “Commercial Items and the Determination of Reasonableness of Price for Commercial Items,” February 4, 2015, and will follow the updates in the DFARS PGI and Commercial Item Handbook when they are published.

Our Response

Comments from the Director, DLA Acquisition, addressed the specifics of the recommendation; therefore, no further comments are required.

Appendix A

Scope and Methodology

We conducted this performance audit from May 2014 through March 2015 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

In July 2014, we informed MABS that we would request commercial and Government sales data and cost data, if necessary, to determine if the contract prices are fair and reasonable. On July 17, 2014, we requested commercial and Government sales data for 79 parts.¹⁸ On August 4, 2014, and August 15, 2014, MABS provided the sales data. On August 28, 2014, we requested cost data for 51 parts. On October 10, 2014, MABS provided 2013 standard labor, material, and overhead costs, and selling, general and administrative expenses to support its costs of the commercial spare parts.

To determine whether DLA purchased sole-source spare parts at fair and reasonable prices from MABS companies, we reviewed contract documentation from March 2, 2012, through November 30, 2014, for contracts SPE4AX-13-D-9418, SPEAX-13-D-9419, and SPEAX-13-D-9420. Specifically, we reviewed:

- contracts;
- modifications;
- delivery orders;
- price negotiation memorandums;
- justification and approval for other than full and open competition;
- acquisition plan; and
- negotiation documentation.

In addition, we reviewed contract documentation from previous MABS contracts SPM4A2-07-D-0006 and SPM4AX-12-D-9423. We interviewed DLA Aviation officials to understand their roles and responsibilities concerning contracts SPE4AX-13-D-9418, SPEAX-13-D-9419, and SPEAX-13-D-9420.

¹⁸ The audit focused on a statistical sample of 54 parts.

We reviewed applicable regulations and guidance on contract pricing, including:

- FAR Subpart 2.1, “Definitions;”
- FAR Subpart 15.4, “Contract Pricing;”
- FAR Clause 52.215-21, “Requirements for Certified Cost or Pricing Data and Data Other Than Certified Cost or Pricing Data;”
- DFARS Subpart 215.4, “Contract Pricing;” and
- DFARS PGI 215.4, “Contract Pricing.”

Sales Analysis for Commercial Parts

We performed sales analysis on the 19 of the 54 parts MABS identified as commercial. Using the MABS companies’ commercial and Government sales data from 2008 through 2012, we performed a sales analysis on the 19 parts to determine which prices were not supported by at least 50 percent commercial sales.

Price Analysis for Commercial of a Type Parts

We performed a price analysis on the 35 of the 54 parts MABS identified as commercial of a type parts. Specifically, we used the sales data from 2008 through 2013 provided for the comparable parts MABS supplied to support the 35 parts as commercial parts. For each of the comparable parts, we identified sales with comparable quantities and prices for each quantity range established on contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420. If the comparable part’s sales data did not contain sales with comparable quantities, we selected the most recent quantity and compared it to the lower quantity range. We inflated all 2008 through 2012 prices to September 2013 levels using Bureau of Labor Statistics Producer Price Index WPU1425–Other Aircraft Parts and Equipment.

Cost Analysis

(FOUO) We conducted cost analysis on 51 of the 54 parts. Using the MABS companies [REDACTED], we calculated a fair and reasonable price. The MABS companies stated [REDACTED]. The MABS companies provided the following further description of their costs.

- (FOUO) [REDACTED]
[REDACTED]
[REDACTED]

- (FOUO) [REDACTED]
[REDACTED]
[REDACTED].
- (FOUO) [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED].
 - (FOUO) [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED].
 - (FOUO) [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED].
 - (FOUO) [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED].

To establish fair and reasonable prices for the contracts' base year, we applied a profit range obtained from the DLA Aviation contracting officer's weighted guidelines calculation. We added the negotiated inflation rate to calculate our fair and reasonable prices for the remaining 4 years of the 2013 contracts. We then compared our calculated prices to the 2013 contracts' prices to determine whether prices were fair and reasonable.

Price Analysis of Quantity Ranges

We performed an analysis of the 140 parts with quantity ranges on contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420. Specifically, we calculated price differences to compare the lowest price to the highest price DLA would have paid for the parts on the 2013 contracts. In addition, we analyzed 152 parts that were included on both contract SPM4AX-12-D-9423 and contract SPE4AX-13-D-9418 to identify 36 parts with new quantity ranges added to contract SPE4AX-13-D-9418 and determined if MABS followed a standard quantity curve.¹⁹

Use of Computer-Processed Data

We assessed the reliability of sales data obtained from the MABS companies' DBA and SAP systems, which are standard enterprise resource planning systems. Specifically, we compared the sales data to a statistical sample of invoices to validate the customers, quantities, and unit prices. Nasco Aircraft Brake and Meggitt Aerospace corrected the errors we identified. Therefore, we determined that the corrected data was sufficiently reliable for the purposes of this audit.

(FOUO) To calculate fair and reasonable prices, we obtained cost data from the MABS companies. According to MABS officials, [REDACTED]
[REDACTED]
[REDACTED]. MABS officials explained
[REDACTED]
[REDACTED]
[REDACTED].

(FOUO) According to MABS officials, [REDACTED]
[REDACTED]
[REDACTED]. To verify the accuracy of the data, we reviewed the
[REDACTED]
[REDACTED] and verified consistent application to all parts for each MABS company. We used the cost data MABS companies provided to calculate fair and reasonable prices and identified differences between the costs to manufacture the parts and the prices the MABS companies charged DoD.

¹⁹ DLA officials stated they use a 95-percent quantity curve to estimate prices. Specifically, they expect a 5-percent decrease in the price when the quantities double.

(FOUO) Officials from the MABS companies stated [REDACTED]
[REDACTED]
[REDACTED]. As a result of this limitation, we referred to calculated overpayments as potential overpayments. Therefore, we determined that the data were sufficiently reliable for the purposes of this audit.

Use of Technical Assistance

We used assistance provided by the DoD OIG Quantitative Methods Division (QMD) during the audit. Specifically, QMD provided a statistical sample of 54 parts on contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-9420 as of July 1, 2014. See Appendix E for a detailed discussion of the statistical sampling methodology.

Appendix B

Prior Coverage

During the last 5 years, the Department of Defense Inspector General (DoD IG) issued 12 reports discussing DoD obtaining parts at fair and reasonable prices. Unrestricted DoD IG reports can be accessed at <http://www.dodig.mil/pubs/index.cfm>.

DoD IG

Report No. DODIG-2015-103, "Summary of DoD Office of Inspector General Spare-Parts Pricing Audits: Additional Guidance is Needed," March 31, 2015

Report No. DODIG-2015-058, "U.S. Air Force May Be Paying Too Much for F117 Engine Sustainment," December 22, 2014

Report No. DODIG-2015-053, "Naval Supply Systems Command Needs to Improve Cost Effectiveness of Purchases for the Phalanx Close-In Weapon System," December 19, 2014

Report No. DODIG-2014-110, "Ontic Engineering and Manufacturing Overcharged the Defense Logistics Agency for Sole-Source Spare Parts," September 15, 2014

Report No. DODIG-2014-106, "Military Sealift Command Oversight of Excess Spare-Parts Inventory and Purchases for Sealift Program Roll-On/Roll-Off Ships Needs Improvement," September 9, 2014

Report No. DODIG-2014-088, "Defense Logistics Agency Aviation Potentially Overpaid Bell Helicopter for Sole-Source Commercial Spare Parts," July 3, 2014

Report No. DODIG-2014-054, "Defense Logistics Agency Land and Maritime Paid Too Much for High Mobility Multipurpose Wheeled Vehicle Repair Parts," April 4, 2014

Report No. DODIG-2014-038, "Air Force Life Cycle Management Center Could Not Identify Actual Cost of F119 Engine Spare Parts Purchased from Pratt and Whitney," February 10, 2014

Report No. DODIG-2014-020, "U.S. Army Contracting Command Did Not Obtain Fair and Reasonable Prices for Communications Equipment," December 5, 2013

Report No. DODIG-2013-090, "Improved Guidance Needed to Obtain Fair and Reasonable Prices for Sole-Source Spare Parts Procured by the Defense Logistics Agency From The Boeing Company," June 7, 2013

Report No. D-2011-104, "Pricing and Escalation Issues Weaken the Effectiveness of the Army Contract with Sikorsky to Support the Corpus Christi Army Depot," September 8, 2011


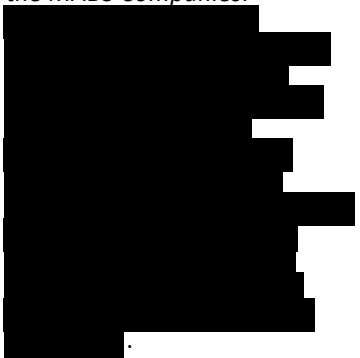
Report No. D-2011-061, "Excess Inventory and Contract Pricing Problems Jeopardize the Army Contract with Boeing to Support the Corpus Christi Army Depot," May 3, 2011

Appendix C

DLA Contracting Officials and DoD OIG Analysis Comparison

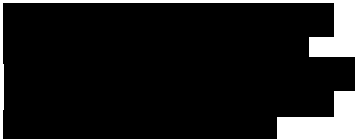



The table below shows the steps contracting officials should follow to obtain and review data, as required by FAR 15.4, “Contract Pricing” and DFARS PGI 215.4, “Contract Pricing,” and the steps and data obtained that DLA contracting officials and the audit team followed to determine whether the prices on the 2013 contracts with the MABS companies were fair and reasonable.

Table C. DLA Contracting Officials and DoD OIG Data Reviewed

(FOUO) FAR 15.4 and DFARS 215.4 Requirements	DLA Contracting Officials' Data Review	Our Data Review
	Part Selection	
		Statistically selected 54 of 182 parts from the contract population as of July 1, 2014.
	Other Than Certified Cost or Pricing Data Reviewed	
Data available to the Government	<i>Previous Prices Paid to the MABS Companies.</i> 	We analyzed the price negotiation memorandums and attachments to understand contracting official's analysis performed to determine fair and reasonable prices.
Data obtained from sources other than the contractor	Contracting officials did not obtain data from sources other than the MABS companies.	We only requested data from DLA Aviation and the MABS companies.

~~(FOUO)~~

Table C. DLA Contracting Officials and DoD OIG Data Reviewed (cont'd)

(FOUO) FAR 15.4 and DFARS 215.4 Requirements	DLA Contracting Officials' Data Review	Our Data Review
Request data from the contractor		We obtained and reviewed technical and commercial sales data from the MABS companies for 54 statistically selected parts.
(a) Commercial Sales Data	The contracting officials reviewed commercial sales data and confirmed that commercial sales existed.	<i>Price Analysis.</i> Performed price analysis on the 35 of 54 parts identified as commercial of a type. We evaluated the sales data for comparable commercial parts that MABS provided to support the prices of the 35 commercial of a type parts on contract. If sales data for the comparable parts did not contain comparable quantities or prices, we requested cost data for the parts on contract. <i>Sales Analysis.</i> We performed sales analysis on the 19 of 54 parts identified as commercial. The sales analysis determined which parts' prices were supported by at least 50 percent commercial sales. If prices were not supported, we requested cost data from the MABS companies.
(b) Additional Data from the contractor	A Defense Contract Management Agency engineer  and issued a report on December 18, 2012, that 	We reviewed the December 18, 2012, Defense Contract Management Agency engineer's report and we conducted a limited review of technical data for commercial of a type parts. We considered the technical data when evaluating the price differences between the comparable and contract parts. We did not use the technical data to determine the commerciality of the contract parts.
If sales data were not sufficient, obtain additional data from the contractor, including cost data	 Contracting officials negotiated contract prices without performing cost analysis on any of the parts reviewed.	As a result of the commercial sales data analysis, we requested and the MABS companies voluntarily provided cost data for the 51 parts. We performed cost analysis to calculate fair and reasonable prices.

(FOUO)

Appendix D

Cost Analysis of Meggitt Aircraft Braking System's Parts

The table below includes the results of the cost analysis for 35 of 51 parts DoD purchased from the MABS companies as of November 30, 2014. We identified approximately \$8.5 million in overpayments for 32 parts and approximately \$0.1 million in underpayments for 3 parts. As of November 30, 2014, DoD had not purchased 16 of the 51 parts reviewed.

Table D. Cost Analysis for 35 Parts

(FOUO) NSN	DLA Contracts ¹			Our Calculated Fair and Reasonable Price		Overpayment/ Underpayment	
	Quantity ²	Weighted Average Unit Price ³	Total Price	Weighted Average Unit Price ⁴	Total Price ⁵	Amount ⁶	Percent ⁶
5330-01-196-2451	173	\$172.88	\$29,908	\$████	████	████	████
5330-01-224-8238	1,346	13.48	18,144	████	████	████	████
1630-01-189-8644	289	936.06	270,521	████	████	████	████
1630-01-037-4960	770	51.32	39,516	████	████	████	████
1630-01-161-4375	199	3,936.77	783,416	████	████	████	████
5365-01-464-9406	5,351	9.52	50,942	████	████	████	████
1630-01-189-8772	94	5,836.76	548,655	████	████	████	████
5330-01-224-8226	424	154.97	65,707	████	████	████	████
1630-01-047-7335	767	2,314.26	1,775,034	████	████	████	████
1630-01-033-4606	1,230	1,371.00	1,686,330	████	████	████	████
1630-01-286-1011	4,000	74.83	299,310	████	████	████	████
1630-01-523-6203	415	1,058.02	439,078	████	████	████	████
1630-01-037-4958	1,000	614.89	614,890	████	████	████	████

(FOUO)

Table D. Cost Analysis for 35 Parts (cont'd)

(FOUO) NSN	DLA Contracts ¹			Our Calculated Fair and Reasonable Price		Overpayment/ Underpayment	
	Quantity ²	Weighted Average Unit Price ³	Total Price	Weighted Average Unit Price ⁴	Total Price ⁵	Amount ⁶	Percent ⁶
1630-01-009-9486	338	3,535.49	1,194,995	██████	██████	██████	██████
4710-01-189-8771	100	2,482.56	248,256	██████	██████	██████	██████
1630-01-005-4188	560	575.00	322,000	██████	██████	██████	██████
1630-00-186-8700	500	516.95	258,475	██████	██████	██████	██████
5310-01-222-4119	300	858.26	257,478	██████	██████	██████	██████
1630-00-937-6602	4,651	464.72	2,161,413	██████	██████	██████	██████
1630-01-345-0479	115	5,806.18	667,711	██████	██████	██████	██████
5330-01-166-2347	200	125.45	25,090	██████	██████	██████	██████
1630-01-009-8474	30	27,440.07	823,202	██████	██████	██████	██████
1630-01-036-3353	217	782.95	169,900	██████	██████	██████	██████
1630-00-032-6102	3,061	365.94	1,120,142	██████	██████	██████	██████
1630-00-186-8702	295	3,716.77	1,096,446	██████	██████	██████	██████
1630-01-003-8538	1,337	404.92	541,378	██████	██████	██████	██████
1630-01-487-6551	141	2,425.27	341,963	██████	██████	██████	██████
1630-01-338-7125	1,308	17.16	22,445	██████	██████	██████	██████
1630-00-186-8697	50	2,600.53	130,027	██████	██████	██████	██████

(FOUO)

Table D. Cost Analysis for 35 Parts (cont'd)

(FOUO) NSN	DLA Contracts ¹			Our Calculated Fair and Reasonable Price		Overpayment/ Underpayment	
	Quantity ²	Weighted Average Unit Price ³	Total Price	Weighted Average Unit Price ⁴	Total Price ⁵	Amount ⁶	Percent ⁶
1630-00-022-3074	1,361	543.13	739,200	████	████	████	████
1650-00-102-4364	13,403	8.26	110,709	████	████	████	████
1630-00-899-5783	3,283	36.06	118,385	████	████	████	████
Total Overpayment⁷ (32 parts)			\$16,970,665		\$8,501,989	\$8,468,676	
1630-99-462-9209	85	\$8,414.27	\$715,213	████	████	████	████
1680-99-776-6758	189	4,779.12	903,254	████	████	████	████
5310-01-258-5953	750	102.55	76,913	████	████	████	████
Total Underpayment⁷ (3 parts)			\$1,695,379		\$ 1,804,723	\$(109,344)	

Note: Numbers in the total price columns and the overpayment/underpayment amount column are rounded to the nearest dollar.

¹ The DLA contracts include contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420.

² The quantity represents DoD purchases as of November 30, 2014.

³ The contracts weighted average unit price represents total price paid for the parts purchased, divided by the quantity purchased.

⁴ The fair and reasonable unit price was calculated using MABS companies direct cost and applying profit to determine a year 1 price. The inflation agreed to in the contracts was applied to determine the year 2 through year 5 prices.

⁵ The fair and reasonable total price represents the weighted average unit price multiplied by the contracts purchased quantity.

⁶ Figures in parenthesis represent negative values.

⁷ Totals do not equal the actual sum because of rounding.

(FOUO)

Appendix E

Sampling Methodology

Sampling Objective

We selected a statistical sample of parts from the population, as described below, for review to determine whether the prices negotiated for those parts were fair and reasonable.

Sample Population

We obtained the parts lists from the MABS 2013 contracts as of July 1, 2014, which included 249 parts. The value of the 249 parts using the estimated annual demand quantities and the appropriate quantity range price for the demands was approximately \$297.9 million. We only included parts with a total purchase price of greater than or equal to \$100,000, which totaled 182 parts valued at approximately \$294.9 million. We considered the 182 parts valued at \$294.9 million as our population.

Sample Design

The DoD OIG QMD designed a stratified sampling plan by dividing the population into three strata (sections) based on the total estimated value of each part. QMD then used Microsoft Excel's random function tool to randomize within each stratum and selected the sample items. See Table E.1 for the number of parts in the statistical sample and population in each stratum.

Table E.1. Strata Used to Select Statistical Sample of Parts

Stratum	Stratum Sample Size (Parts)	Sample Total Value	Stratum Population Size (Parts)	Population Total Value
Greater than or equal to \$2 million	29	\$204,629,726	29	\$204,629,726
Greater than or equal to \$450,000 and less than \$2 million	15	13,201,656	78	71,413,477
Greater than or equal to \$100,000 and less than \$450,000	10	2,168,599	75	18,845,851
Total	54	\$219,999,982	182	\$294,889,055

Sample Results

Table E.2 shows the \$8.5 million overpayment results, by stratum, for the 32 sample items that DoD purchased from the MABS companies as of November 30, 2014.

Table E.2. Potential Overpayment as of November 30, 2014

Stratum	Number of Overpayments	Sample Total Value	Total Overpayment
Greater than or equal to \$2 million	17	\$14,890,786	\$7,528,992
Greater than or equal to \$450,000 and less than \$2 million	10	1,933,350	852,220
Greater than or equal to \$100,000 and less than \$450,000	5	146,529	87,465
Total	32	\$16,970,665	\$8,468,676

Table E.3 shows the \$70.5 million overpayment results, by stratum, DLA Aviation may potentially overpay the MABS companies over the remaining term of the contract for 47 sample items.

Table E.3. Potential Overpayment from December 1, 2014, through August 31, 2018

Stratum	Number of Overpayments	Sample Total Value	Total Overpayment
Greater than or equal to \$2 million	25	\$146,645,663	\$64,931,773
Greater than or equal to \$450,000 and less than \$2 million	14	9,776,151	4,818,449
Greater than or equal to \$100,000 and less than \$450,000	8	1,418,012	794,134
Total	47	\$157,839,826	\$70,544,356

Sample Projections

Based on the sample results, Table E.2 shows the potential overpayment paid to MABS companies as of November 30, 2014, and the potential overpayment DLA may pay MABS companies for the remainder of the contract. To interpret the projections listed below, we are 90 percent confident that DLA potentially overpaid MABS companies for spare parts between \$10,495,213 and \$14,464,141 as of November 30, 2014, and will potentially overpay between \$86,608,367 and \$101,957,111 for the remainder of the contract. The point estimates, or middle point between the low and upper bounds, are \$12,479,677 and \$94,282,739, respectively. We used the combined point estimate in the Finding.

Table E.4. Statistical Projection Results

Category	Potential Overpayment (Lower Bound)	Potential Overpayment (Point Estimate)	Potential Overpayment (Upper Bound)
Potential Overpayment as of November 30, 2014	\$10,495,213	\$12,479,677	\$14,464,141
Potential Overpayment DLA May Pay, December 1, 2014 through August 31, 2018	86,608,367	94,282,739	101,957,111
Combined Projections	\$98,835,621	\$106,762,416	\$114,689,212

Management Comments

Defense Pricing



ACQUISITION,
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

APR 22 2015

MEMORANDUM FOR PROGRAM DIRECTOR, ACQUISITION, PARTS, AND
INVENTORY, OFFICE OF INSPECTOR GENERAL

THROUGH: DIRECTOR, ACQUISITION RESOURCES AND ANALYSIS *7C-122/15*

SUBJECT: Response to DoDIG Draft Report on Defense Logistics Agency Did Not Obtain Fair
and Reasonable Prices From Meggitt Aircraft Braking Systems for Sole-Source
Commercial Spare Parts (Project No. D2014-D000AH-0180.000)

As requested, I am providing responses to the recommendations contained in the subject
report.

Recommendations 1.a and 1.b:

The Office of the Inspector General recommends that the Director, Defense Pricing:

- a. Issue guidance to establish a percentage of commercial sales that is sufficient to determine fair and reasonable prices when commercial items are acquired on a sole-source contract.
- b. Assess and issue guidance prohibiting contracting officers from placing clauses in sole-source commercial contracts limiting their ability to obtain cost data.

Response 1.a:

Concur. The Director, Defense Pricing and Acting Director, Defense Procurement and Acquisition Policy (DPAP) are developing a proposed Defense Federal Acquisition Regulation Supplement (DFARS) rule (Case 2013- D0034, Evaluating Price Reasonableness for Commercial Items) in which we plan to include a definition of "Market-based pricing." We anticipate that this definition will include a percentage of commercial sales that is sufficient to determine fair and reasonable prices when commercial items are acquired on a sole-source contract.

Response 1.b:

Concur. DPAP plans to include language in the same proposed DFARS rule to prohibit contracting officers from placing clauses in sole-source commercial contracts limiting their ability to obtain cost data. It is our intent that the text will comply with the DoDIG report's recommendations.

Please contact [REDACTED] if additional
information is required.

[Signature]
Shay D. Assad
Director, Defense Pricing

Defense Logistics Agency



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD
FORT BELVOIR, VIRGINIA 22060-6221

APR 10 2015

MEMORANDUM FOR THE DEPARTMENT OF DEFENSE INSPECTOR GENERAL

SUBJECT: Response to DoD IG Draft Report "Defense Logistics Agency Did Not Obtain Fair and Reasonable Prices From Meggitt Aircraft Braking Systems for Sole-Source Spare Parts," (Project No. D2014-D000AH-0180.000)

Attached is the Defense Logistics Agency's (DLA) response to the subject Draft Report. We appreciate the opportunity to review and comment on the finding and recommendations. We would like to also take this opportunity to provide an update on various initiatives DLA has implemented because of findings from recent DoD IG Audits.

First, in December 2014 DLA Acquisition issued "Guidance on Determining Sole Source Commercial Prices Fair and Reasonable," which established a 40% non-Government sales threshold as a sufficient percentage of sales to support fair and reasonable price determinations. The Guidance further established a requirement that there be at least five sales in the prior three years as the basis in using commercial sales for price reasonableness determinations.

Second, DLA performed an in-depth review of 192 contract files to evaluate the adequacy of the cost and/or price analysis and documentation used to support fair and reasonable prices for the acquisition of sole-source spare parts. The results of the review showed specific areas where additional education and training are needed in the acquisition workforce. As a result, DLA Acquisition collaborated with the Defense Acquisition University to create a DLA specific cost/price training course. The course, "Determining Price Reasonableness Using Price or Cost Analysis Methods" focuses on areas including market research, sole-source commercial pricing, price/cost analysis techniques, escalation methods and analysis and learning curves.

Finally, DLA is currently in the process of creating an in-house Enterprise Pricing Tool Suite (EPTS) that will provide support tools to the workforce for cost/price analysis. The EPTS will include weighted guidelines, price indices, pricing history analysis on specified NSNs with a cost graph, and rare metal market price volatility.

The point of contact for this audit is [REDACTED] DLA Office of the Inspector General, [REDACTED]


MATTHEW R. BEEBE
Director, DLA Acquisition

Attachment:
As stated

Defense Logistics Agency (cont'd)

2

The Department of Defense Inspector General recommends that the Director, Defense Logistics Agency (DLA):

Recommendation 2.a: Review the performance of the DLA Aviation contracting officer (KO) for contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420 to determine if sufficient price analysis was conducted and if inclusion of language in the contracts restricting cost data limited DLA's ability to determine fair and reasonable prices. Based on the results of the review of the KO's actions, initiate administrative action, as appropriate.

DLA Response 2a: Concur. During the course of this audit, the Director, DLA Acquisition reviewed the pricing-related documents on the three Meggitt Aircraft Braking Systems (MABS) contracts and determined sufficient price analysis was conducted to properly determine the prices fair and reasonable. The documentation shows the contracting officer was correct in his review and methodology used in price analysis, establishing negotiation objectives, negotiating prices, documenting detailed information on the negotiations, and determining the prices as fair and reasonable. Also, as discussed in response to recommendation 2.c below, the Director, DLA Acquisition determined the language included in paragraph (b) of clause 52.215-21, Alt IV, Requirements for Certified Cost or Pricing Data and Data Other Than Certified Cost or Pricing Data -- Modifications (Oct 2010), did not limit DLA's ability to determine fair and reasonable prices. Therefore, no action is required.

Recommendation 2.b: Establish a quality assurance process to ensure when requests for contractor data is denied, KOs follow the procedures in Defense Federal Acquisition Regulation Supplement Procedures, Guidance, and Information (DFARS PGI) 215.404-1(a), which requires contracting officials to elevate data request denials to the appropriate level to resolve the problem, including the Head of the Contracting Activity (HCA).

DLA Response 2b: Concur. DLA has a quality assurance process in place in the DLA Acquisition Directive (DLAD), 15.405(a)(S-90),

The offeror's refusal to provide . . . information other than cost or pricing data does not relieve the KO from the requirement to perform a proposal analysis . . . for determining the prices . . . fair and reasonable In such instance, the guidance in 15.404-2(d) applies.

DLAD 15.404-2(d)(S-90) states that,

In the event the efforts of the KO and higher management are unsuccessful in obtaining the data, the matter shall be elevated, after review by the local pricing and contract review elements to the Head of the Contracting Activity (HCA), along with the information in (1) through (14).

DODIG PROJECT NO. D2014-D000AH-0180.000

Defense Logistics Agency (cont'd)

3

The information in 1-14 includes such areas as the offeror's written refusal, a summary of attempts to secure data and the results, substantiation that the item is mission essential, and alternatives to proceeding with the acquisition and suggested courses of action considering the alternatives. With regard to the present audit findings, since the contracting officer properly determined the prices were fair and reasonable through price analysis, the process in DFARS PGI 215.404-1(a) was not applicable.

Recommendation 2.c: Assess contract clause 52.215-21, "Requirements for Certified Cost or Pricing Data and Data Other Than Certified Cost or Pricing Data," included in contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420 and determine whether the statement, "cost data of any kind is not required under this contract," is appropriate and, if not, initiate actions as necessary that requires the DLA Aviation KO to modify the contracts to remove the statement.

DLA Response 2c: Concur. DLA assessed the statement "cost data of any kind is not required under this contract," and determined the language is appropriate in the circumstances of this procurement. The FAR clause expressly authorizes the contracting officer to insert language to describe the data required, and the clause and applicable regulatory guidance, such as FAR 15.404-1(a)(2) and (4), leaves to his discretion the type of data to be submitted. Neither the clause nor applicable regulations require that the data must include "cost" data. The language used by the contracting officer simply reflected the parties' agreement that they would add to the contracts only commercial items for which prices could be determined fair and reasonable based on sales data, without the need to resort to cost data. Consistent with this approach, the contracting officer inserted into the clause specific requirements for data to be submitted by MABS, as follows:

(b) Provide the data described below:

MABS will provide other than cost and pricing data including, but not limited to, commercial sales history, technical comparisons, and narrative explanations, only for items with an estimated annual demand value greater than the simplified acquisition threshold, and only at the contracting officer's request. Cost data of any kind is not required under this contract.

[Italicized language was inserted by the contracting officer]

Since the language is appropriate and the contracting officer obtained sufficient non-cost data to properly determine the prices fair and reasonable, no action is necessary that requires negotiations with MABS to modify the contracts to remove the statement.

Recommendation 2.d: Require the DLA Aviation KO to establish fair and reasonable pricing for future parts added to contracts SPE4AX-13-D-9418, SPE4AX-13-D-9419, and SPE4AX-13-D-9420, and all future sole-source contracts with MABS for commercial parts to include performing a thorough review of prior prices, sales data, and requesting other than certified cost or pricing data, to include cost data when commercial sales data are not sufficient to determine fair and reasonable prices for sole-source commercial parts.

DODIG PROJECT NO. D2014-D000AH-0180.000

Defense Logistics Agency (cont'd)

4

DLA Response 2d: Concur. DLA contracting personnel will follow all current and future applicable FAR, DFARS, and DLAD policies and procedures to establish fair and reasonable pricing for future parts added to the MABS contracts and all future sole-source contracts with MABS for commercial parts. This includes DLA's "Guidance on Determining Sole Source Commercial Prices Fair and Reasonable," dated December 16, 2014. DLA will consider requesting assistance from the Defense Contract Management Agency Cost & Pricing Center for future acquisitions. DLA will continue to negotiate with MABS on all future parts added to these contracts and on all future contracts with MABS. DLA will also follow the Office of the Under Secretary of Defense, Acquisition Technology and Logistics Memorandum, "Commercial Items and the Determination of Reasonableness of Price for Commercial Items," dated February 4, 2015. When published, DLA will follow the updates in the DFARS PGI and Commercial Item Handbook, also referenced in the Memorandum.

DODIG PROJECT NO. D2014-D000AH-0180.000

Acronyms and Abbreviations

DFARS	Defense Federal Acquisition Supplement
DLA	Defense Logistics Agency
FAR	Federal Acquisition Regulation
MABS	Meggitt Aircraft Braking Systems
PGI	Procedures, Guidance, and Information
QMD	Quantitative Methods Division



Whistleblower Protection

U.S. DEPARTMENT OF DEFENSE

The Whistleblower Protection Enhancement Act of 2012 requires the Inspector General to designate a Whistleblower Protection Ombudsman to educate agency employees about prohibitions on retaliation, and rights and remedies against retaliation for protected disclosures. The designated ombudsman is the DoD Hotline Director. For more information on your rights and remedies against retaliation, visit www.dodig.mil/programs/whistleblower.

For more information about DoD IG reports or activities, please contact us:

Congressional Liaison

congressional@dodig.mil; 703.604.8324

Media Contact

public.affairs@dodig.mil; 703.604.8324

Monthly Update

dodigconnect-request@listserve.com

Reports Mailing List

dodig_report@listserve.com

Twitter

twitter.com/DoD_IG

DoD Hotline

dodig.mil/hotline

~~FOR OFFICIAL USE ONLY~~



DEPARTMENT OF DEFENSE | INSPECTOR GENERAL

4800 Mark Center Drive
Alexandria, VA 22350-1500
www.dodig.mil
Defense Hotline 1.800.424.9098

~~FOR OFFICIAL USE ONLY~~